

Office of Chief Counsel  
Internal Revenue Service

**memorandum**

CC:SER:GCD:NO:TL-N-6704-99  
SSCanavello

date: **10 DEC 1999**

to: Associate Chief, Appeals Division  
Gulf Coast District, Birmingham, AL

from: District Counsel, Gulf Coast District, New Orleans

subject: Advisory Opinion - [REDACTED]

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**ISSUE**

Whether the taxpayer estate is entitled to a deduction based upon an obligation to account for the usufruct of a one-half interest in Series HH United States Savings Bonds.

**CONCLUSION**

The taxpayer estate has no obligation to account for a usufruct of one-half of the savings bonds, because the decedent had full ownership of the bonds at the date of death.

**FACTS**

The bonds in question are as follows:

- (1) \$ [REDACTED] of Series E United States Savings Bonds issued in the name of "[REDACTED]";
- (2) \$ [REDACTED] of Series E United States Savings Bonds issued in the name of "[REDACTED] and [REDACTED]"; and

- (3) \$ [REDACTED] of Series EE United States Savings Bonds issued in the name of "[REDACTED]"

Your memorandum indicates that these bonds were acquired during the marriage of decedent and [REDACTED]. Since the protest indicates that they were "held as community property", we assume that decedent and [REDACTED] were subject to the community property regime throughout their marriage.

[REDACTED] died on [REDACTED]. The protest states that in her will she bequeathed to her husband a usufruct for life or until remarriage over her interest in these bonds. The protest further states that [REDACTED] was placed in possession of [REDACTED] of the bonds as surviving spouse in community and as usufructuary over the other undivided one-half interest.

You indicate in your memorandum that the bonds were subsequently sold by [REDACTED] and converted into other assets, primarily Series HH United States Savings Bonds. You further state that the value of the HH Bonds was included in his estate. Decedent's estate has claimed a deduction, based upon a usufructuary accounting obligation to the naked owners (the two children of [REDACTED]), in the amount of \$ [REDACTED], which represents one-half of the total value of all the bonds, both the ones registered in decedent's name alone and the ones registered in his and [REDACTED]'s names.

#### DISCUSSION

United States Savings Bonds are issued under the authority of 31 U.S.C. §3105, and the rules governing their issuance and transfer are set forth in the Code of Federal Regulations (CFR). 31 CFR §353.5 states that savings bonds are issued only in registered form, that the registration must express the actual ownership of, and interest in, the bond, and that registration is conclusive of ownership, except that, pursuant to 31 CFR §353.49, a bond "may be reissued to correct an error in registration upon appropriate request supported by satisfactory proof of the error."

The courts have addressed on numerous occasions the problem that arises when the ownership of savings bonds as determined under federal law conflicts with the ownership of those bonds as determined under state law. The question has arisen more than once in the context of bonds issued in the name of both spouses

residing in a community property state. Upon the death of one spouse, state law treats the bonds as belonging one-half to the surviving spouse and one-half to the heirs of the deceased spouse, whereas federal law treats the bonds as belonging entirely to the surviving spouse under the survivorship provisions of the CFR.

This type of conflict was at issue in Free v. Bland, 369 U.S. 663, 82 S.Ct. 1089 (1962); United States v. Chandler, 410 U.S. 257, 93 S.Ct. 880 (1973); and Cooper v. United States, 429 F.2d 535 (W.D. La. 1974). In each of those cases, the reviewing court applied the principle that, under the Supremacy Clause of the United States Constitution, federal law must prevail where it conflicts with state law.

In the present case, the \$[REDACTED] of bonds issued in the names of both spouses belonged to [REDACTED] as survivor in full ownership upon [REDACTED]'s death, based upon the cases cited in the preceding paragraph.

The decedent's estate attempts in its protest to distinguish the bonds issued in decedent's name only from bonds of the type considered in Free, Chandler, and Cooper. 31 U.S.C. §353.5, however, makes no such distinction. It merely states that registration is conclusive of ownership and must express the actual ownership of an interest in the bond, except where there has been an error in registration. No such error has been alleged in this case.

Nor has fraud or breach of trust been alleged in this case. The United States Supreme Court stated in Free that "[t]he regulations are not intended to be a shield for fraud and relief would be available in a case where the circumstances manifest fraud or a breach of trust tantamount thereto on the part of a husband while acting in his capacity as manager of the general community property." 369 U.S. at 670.

The United States Supreme Court found an example of such fraud or breach of trust in Yiatchos v. Yiatchos, 376 U.S. 306, 84 S.Ct. 742 (1964), decided two years after Free v. Bland. In Yiatchos, bonds were purchased with community property by the husband and registered in his name only, and naming his brother as beneficiary, during a time when state law provided that the husband was the manager of the community. The Court allowed the brother to keep the one-half interest in the bonds formerly held by the decedent husband, and remanded the case as to the other one-half interest (belonging to the wife under community property law).

We have not been provided with information about when the various bonds were bought, so as to determine whether any or all of them were purchased at a time when, under Louisiana law, the husband was head and master of the community. Thus, we cannot give an opinion as to whether there is a possible "breach of trust" argument in this case. Nor has any evidence of fraud against the wife been asserted in this case. It simply appears that, for whatever reason, bonds purchased during the existence of the community were registered in the name of decedent alone. We also note that no information has been made available as to whether the funds used to purchase the bonds were community or separate, so we must follow the presumption under Louisiana community property law that all property acquired during the existence of the community is community property.

The estate argues in its protest that Free, Chandler and Cooper are inapplicable because the bonds were issued in the name of decedent only, whereas those cases involved survivorship rights created by the form of registration of the bonds under federal law. In support of that proposition, the estate cites 31 CFR §353.70(a) and §353.71 as directing that the disposition of the bonds would have to be in accordance with state law.

We disagree with this conclusion. Section 353.70(a) states that "[i]f the owner of a bond registered in single ownership form has died, the bond becomes the property of that decedent's estate ...." This supports the Service's position, that the bonds belonged to decedent in full ownership because they were registered to him alone. Section 353.71 provides the method for requesting payment or reissue of bonds included in a decedent's estate "... in the names of the persons entitled to share in the estate ...." It does not direct the disposition of the bonds, but merely tells the legal representative of the estate what is necessary in order to have the bonds reissued.

Finally, the estate has made the argument in its protest that decedent's sale of the bonds converted them into cash and therefore converted the usufruct of nonconsumables into a usufruct of consumables, creating an obligation to account for one-half of the sales proceeds. The protest states that at the death of the decedent, he did not own savings bonds at all. This conflicts factually with the statement in your memorandum that decedent purchased Series HH bonds with some or all of the proceeds, and that the Series HH bonds were included on his estate tax return. I suggest that this discrepancy be clarified.

Nevertheless, since we conclude that decedent never had a usufruct over any interest in the bonds, but rather owned them in full ownership, the issue of whether the alleged usufruct was converted from one of nonconsumables to one of consumables is irrelevant.

If you have further questions or require additional assistance please call Susan Canavello at (504) 556-3114. We are available to review any notice of deficiency which may be issued with respect to this issue, and further suggest that you determine whether any tax has already been paid on the bonds in [REDACTED]'s estate.

(Signed) Susan S. Canavello

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cc: Shelli Stump